

REPORT OF THE AUDITOR-GENERAL TO THE NORTHERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON HANTAM LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Hantam Local Municipality set out on pages 10 to 61, which comprise the statement of financial position as at 30 June 2014, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information with actual information for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting Officer's responsibility for the separate financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2013 (Act No. 2 of 2013) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Hantam Local Municipality as at 30 June 2014 and its financial performance and cash flows for the year then ended, in accordance with the SA Standards of GRAP and the requirements of the requirements of the MFMA and the DoRA.



Emphasis of matters

7. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

8. As disclosed in note 46 to the financial statements, the corresponding figures for 30 June 2013 have been restated as a result of an error discovered during 2014 in the financial statements of the municipality at, and for the year ended, 30 June 2013.

Material losses/impairments

9. As disclosed in note 16 to the financial statements, a significant provision for the impairment of receivables from exchange transactions was made which constitutes R18 524 343 the total receivables from exchange transactions balance.
10. As disclosed in note 17 to the financial statements, a significant provision for the impairment of receivables from non-exchange transactions was made which constitutes R4 723 079 total receivables from non-exchange transactions balance.
11. As disclosed in note 44 to the financial statements, material losses to the amount of R3 235 378 were incurred as a result of the distribution of electricity.

Additional matter

12. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited supplementary information

13. The supplementary information set out on appendixes A to E does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

Unaudited disclosure notes

14. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

15. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report, non-compliance with legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

16. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected objectives presented in the annual performance report of the municipality for the year ended 30 June 2014:
 - KPA 2: Basic Service Delivery on pages 51 to 195.
 - KPA 5: Good Governance and Public Participation on pages 51 to 195.



17. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
18. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned objectives. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).
19. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
20. The material findings in respect of the selected objectives are as follow:

KPA 2: Basic Service Delivery

Usefulness of reported performance information

21. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. The relevance of the indicators could not be assessed due to a lack of corroborative supporting evidence to verify management's explanation why the indicators were considered important and relevant to the realisation of strategic goals and objectives.
22. The FMPPI requires the following:
 - Performance targets must be specific in clearly identifying the nature and required level of performance and must be measurable and the period or deadline for delivery of targets must be specified.
 - Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. Performance indicators must also be verifiable.
23. The measurability of planned targets and indicators could not be assessed due to a lack of technical indicator descriptions, proper systems and processes and formal standard operating procedures or documented system descriptions.

Reliability of reported performance information

24. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. We were unable to obtain the information and explanations we considered necessary to satisfy ourselves as to the reliability of the reported performance information. This was due to limitations placed on the scope of our work due to the absence of information systems, the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and the lack of usefulness of the indicators and targets.

KPA 5: Good Governance and Public Participation

Usefulness of reported performance information

25. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. A total of 29% of



the indicators did not relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives as per the three-year strategic plan. This was because proper performance planning and management practices had not been implemented to provide for the development of performance indicators and targets included in the annual performance strategic plan.

26. The FMPPi requires the following:

- Performance targets must be specific in clearly identifying the nature and required level of performance must be measurable and the period or deadline for delivery of targets must be specified, and
- Performance indicators/measures must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. Performance indicators/measures must also be verifiable.

27. The measurability of planned targets and indicators could not be assessed due to a lack of technical indicator descriptions, proper systems and processes and formal standard operating procedures or documented system descriptions.

Reliability of reported performance information

28. The FMPPi requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. We were unable to obtain the information and explanations we considered necessary to satisfy ourselves as to the reliability of the reported performance information. This was due to limitations placed on the scope of our work due to the absence of information systems, the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and the lack of usefulness of the indicators and targets.

Achievement of planned targets

29. Refer to the annual performance report on pages 51 to 195 for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information for the selected objectives reported in paragraphs 18 to 25 of this report.

Compliance with legislation

30. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Strategic planning and performance management

31. The local community was not consulted by means of a municipal wide structure for community participation or through a forum that enhances community participation in drafting and implementing the Integrated development plan (IDP), as required by section 28 of the MSA and Municipal Planning and Performance Management Regulation 15(1)(a)(i).

32. The IDP was not annually reviewed based on the assessment of its performance measurements or changing circumstances, as required by section 34 of the MSA and Municipal Planning and Performance Management Regulation 3 and 11.
33. The performance management system
 - did not clarify the roles and responsibilities of each role-player; and
 - did not determine the frequency of reporting and the lines of accountability; and
 - did not relate to the employee's performance management processes as required by section 38(a) of the MSA and Municipal Planning and Performance Management Regulation 7(2)(c to g).
34. Measurable performance targets for the financial year with regard to each of the development priorities or objectives and key performance indicators were not set in the IDP, as required by section 41(1)(b) of the MSA and the Municipal Planning and Performance Management Regulation 12(1) and 12(2)(e).
35. The annual performance report for the year under review did not include a comparison of the performance with set targets and a comparison with the previous financial year and measures taken to improve performance, as required by section 46 (1)(b) of the MSA.

Budgets

36. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.
37. Expenditure was approved as unforeseen and unavoidable which was considered by the council but not included in the approved annual budget, in contravention of Municipal Budget and Reporting Regulation 71(2).

Annual financial statements and annual report

38. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA.
39. Material misstatements of non-current assets, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statement were subsequently corrected and the supporting records were provided subsequently, resulting in the financial statements receiving an unqualified audit opinion.

Expenditure management

40. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure, fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Asset management

41. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Consequence management

42. Unauthorised and irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.



43. The condonation of irregular expenditure was not approved by the appropriate relevant authority, as required by section 1 and 170 of the MFMA.

Procurement and contract management

44. Sufficient appropriate audit evidence could not be obtained that bid specifications for procurement of goods and services through competitive bids were drafted in an unbiased manner that allowed all potential suppliers to offer their goods or services, as per required by SCM Regulation 27(2)(a).
45. Bid specifications were not always drafted by bid specification committees which were composed of one or more officials of the municipality as required by SCM Regulation 27(3).
46. Sufficient appropriate audit evidence could not be obtained that contracts were awarded to bidders based on points given for criteria that were stipulated in the original invitation for bidding, as required by SCM Regulations 21(b) and 28(1)(a) and Preferential Procurement Regulations.
47. Bid adjudication was not always done by committees which were composed in accordance with SCM Regulation 29(2).
48. Construction contracts were awarded to contractors that were not registered with the Construction Industry Development Board (CIDB), in accordance with section 18(1) of the CIDB Act.
49. Construction projects were not always registered with the CIDB, as required by section 22 of the CIDB Act and CIDB Regulation 18.

Grants

50. The Municipal Infrastructure Grant allocation was not spent in accordance with the applicable grant framework, in contravention of section 16(1) of the DoRA.
51. Municipal Infrastructure Grant funds were retained to the next financial year without seeking the approval of the National Treasury, as required by sections 21(1) of the DoRA.
52. The municipality did not evaluate its performance in respect of programmes or functions funded by the Municipal Systems Improvement Grant allocation, as required by section 12(5) of the DoRA.
53. Municipal Systems Improvement Grant funds were retained to the next financial year without seeking the approval of the National Treasury, as required by sections 21(1) of the DoRA.
54. The municipality did not evaluate its performance in respect of programmes or functions funded by the Local Government Financial Management Grant allocation, as required by section 12(5) of the DoRA.

Internal control

55. I considered internal control relevant to my audit of the financial statements, section 47 performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified opinion, the findings on the section 47 performance report and the findings on non-compliance with legislation included in this report.



Leadership

56. The accounting officer did not exercise adequate oversight responsibility over the preparation of the financial statements, the report on predetermined objectives, compliance with laws and regulations, and internal control. The leadership did not implement processes to ensure that reviews took place before information was submitted. This was also evidenced by the material misstatements in the financial statements, non-compliance with laws and regulations and internal control deficiencies noted throughout the audit process.

Financial and performance management

57. Manual or automated controls were not designed to ensure that the transactions had occurred, were authorised and were completely and accurately processed in all instances, while the system of internal control was not adequately designed. Certain corrective measures were not implemented to address the shortcomings in the financial statements and related systems.
58. Material amendments had to be made to the financial statements as these were not accurate and complete, because senior management did not pick up inconsistencies during the review process. This indicates that there were weaknesses in internal control with regard to the review process of the financial statements.
59. There were deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.

Governance

60. The internal audit unit did not conduct internal audits or reviews of performance information systems and management thereof that focused on compliance aspects as well as the usefulness and reliability of the reported performance information.

*Auditor - General
Kimberley*

30 November 2014



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